Supreme Court, U.S.
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No. 01-1078

IN THE

Supreme Court Of The United States

Beverly Burden, Chapter 13 Trustee for the Estates of Luther Gilbert, Jr., Victoria Tevis, Santina Turner, and Frank Lewis Bradshaw; and Francine Jackman, Elaine Steward Greene, Luther Gilbert, Jr., Victoria Tevis, Santina Turner, and Frank Lewis Bradshaw, Individually

Petitioners,

v.

Check Into Cash of Kentucky, LLC, W. Allan Jones, Jr. and Unknown Entities and Individuals

Respondents,

v.

Commonwealth of Kentucky, Department of Financial Institutions,

Third-Party Respondent

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

PETITIONERS' REPLY TO BRIEF IN OPPOSITION

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ARGUMENT

As explained in our petition for *certiorari*, this case presents the question of whether the Federal Arbitration Act, 9 U.S.C. §§ 1-16, requires parties to arbitrate an allegation that the entire contract containing an arbitration clause is void *ab initio* and therefore never came into existence and never had legal effect. Check Into Cash's primary argument in response is that this question is answered by the holding in *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967), that an allegation of fraud in the inducement of a contract (which would render the contract *voidable*, but not void) is subject to arbitration. *See* Opp. at 7-9. This response only begs the question, however, because the scope of *Prima Paint* and whether it extends to allegations that a contract is void *ab initio* is precisely the issue over which federal and state appellate courts are deeply divided. Check Into Cash's attempt to harmonize the disparate appellate decisions interpreting the scope of *Prima Paint*, much like the attempt made by the Sixth Circuit below, only highlights the need for this Court's review.

I. The Decision Below Conflicts with Federal and State Appellate Authority on whether *Prima Paint* Applies to Allegations that a Contract is Void *Ab Initio*.

Check Into Cash attempts to reconcile the split among courts of appeals on whether *Prima Paint* extends to allegations that a contract is void *ab initio* by distinguishing between voidness allegations based on lack of signatory authority and those based on illegal contract terms. Opp. at 14-16. This proposed distinction does not reconcile the split, however, because the ruling below applies *Prima Paint* to *both* types of voidness allegations, while other courts have reasoned that *Prima Paint* does not apply to *any* allegation that a contract is void. There is thus a significant split between the ruling below and those federal and state court decisions cited in both parties'

briefs holding that *Prima Paint* does not apply to allegations that a contract is void *ab initio* based either on a party's lack of signatory authority or on its illegal terms.

Contrary to Check Into Cash's assertion, Opp. at 15-16, Petitioners are challenging a party's signatory authority in this case and the court below held that these allegations must be submitted to arbitration. *See* Cert. App. 12. Petitioners argued in the proceedings below that there was never a valid contract between the parties in part because Check Into Cash was not licensed to enter into the transactions at issue under the Kentucky Business Code, KY. REV. STAT. ANN. § 288.420 (Banks-Baldwin 2001). The Sixth Circuit recognized that this is a challenge to a party's signatory power, noted that the Ninth Circuit in *Three Valleys Mun. Water Dist. v. E.F. Hutton & Co., Inc.*, 925 F.2d 1136 (9th Cir. 1991), held that a court must resolve such challenges before it can enforce an arbitration clause, but nonetheless ordered Petitioners to submit this claim to arbitration. Cert. App. 12. Any distinction between challenges to signatory authority and challenges to a contract's facial legality thus does not erase the split of authority over the scope of *Prima Paint* that the decision below implicates.

Furthermore, Check Into Cash's distinction among the different bases for finding a contract void *ab initio* ignores the reasoning of the various courts that, contrary to the Sixth Circuit below, have limited *Prima Paint* to allegations that a contract is voidable. In *Sandvik AB v. Advent Int'l Corp.*, 220 F.3d 99 (3d Cir. 2000), for example, the Third Circuit held that:

> Mindful of the doctrine announced in *Prima Paint*, which did not consider a situation in which the *existence* of the underlying contract was at issue, we draw a distinction between

> contracts that are asserted to be 'void' or non-existent, as is contended here, and those that are merely 'voidable,' as was the contract at issue in *Prima Paint*, for purposes of evaluating whether the making of an arbitration agreement is in dispute.

Id. at 107 (emphasis added). Likewise, the Ninth Circuit in *Three Valleys* held that "*Prima Paint* applies to 'voidable' contracts," while "a party who contests the making of a contract containing an arbitration provision cannot be compelled to arbitrate the threshold issue of the *existence* of an agreement to arbitrate." *Three Valleys*, 925 F.2d at 1140-41 (emphasis in original). *Sandvik* and *Three Valleys* both hold that allegations that an underlying contract is void or non-existent bring into question the "making of the agreement for arbitration," 9 U.S.C. § 4, and therefore must be decided by a court.[1] Under these holdings, Petitioners' allegations that Check Into Cash lacked authority to enter into the payday loan contracts at issue *and* that these contracts are illegal and void on their face would be resolved by a court, and not through arbitration as the Sixth Circuit ordered. This Court should grant review to resolve this split among the circuit courts over the scope of *Prima Paint*.

Check Into Cash's attempt to explain away the conflict between the ruling below and the state court opinions applying the FAA that are discussed in the parties' briefs is likewise unavailing. Check Into Cash speculates, for example, that the decision in *Alabama Catalog Sales v. Harris*, 794 So.2d 312 (Ala. 2000), does not involve an application of the FAA even

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[1] Thus, it is not "undisputed" that Petitioners never put the making of the arbitration clause into issue. Opp. at 11. The allegation that the entire contract is void *ab initio* puts the making of the arbitration clause into issue.

though "the contract in that case referenced the Federal Arbitration Act and the court referenced several federal decisions under the FAA." Opp. at 16-17. It is a virtual certainty that *Harris* applied the FAA because, as Check Into Cash acknowledges, applicable state law in that case would have prohibited enforcement of *any* arbitration agreement without regard to the question presented. *See* Opp. at 17, citing Ala. Code § 8-1-41(3). *Harris* therefore must have applied the FAA in order even to reach the arbitrability question at issue in that case and in the instant case.[2]

As an application of the FAA, *Harris* undermines Check Into Cash's distinction between voidness allegations based on signatory authority and those based on illegal contract terms as a basis to resolve the split of authority. The *Harris* plaintiffs argued that the defendant's entire payday loan contract was void *ab initio* because it was illegal under Alabama's Small Loan Act. *Harris*, 794 So.2d at 313-14. This is nearly identical to Petitioners' claim that Check Into Cash's payday loan contracts are void because they are illegal under Kentucky's consumer loan statute, which provides that "[a]ny loan contract made in

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[2] Since *Harris* applied the FAA, the conflict with the instant case cannot be explained by an allegedly "unique hostility to arbitration generally" on the part of the *Harris* court. *See* Opp. at 17. In fact, the Alabama Supreme Court has repeatedly been willing to apply the FAA and enforce arbitration contracts despite the existence of countervailing state law. *See, e.g., Southern Energy Homes, Inc. v. Ard*, 772 So.2d 1131 (Ala. 2000) (requiring arbitration of claims under federal Magnuson-Moss Warranty Act); *American Bankers Ins. Co. v. Crawford*, 757 So.2d 1125 (Ala. 1999) (enforcing arbitration clause in insurance contract); *McDougle v. Silvernell*, 738 So.2d 806 (Ala. 1999) (enforcing arbitration clause in insurance contract as invoked by non-signatory defendant as third party beneficiary of contract); *Robert Frank McAlpine Architecture, Inc. v. Heilpern*, 712 So.2d 738 (Ala. 1998) (enforcing arbitration clause in employment contract).

violation of this chapter *shall be void and the lender shall have no right to collect any principal, charges or recompense whatsoever.*" KY. REV. STAT. ANN. § 288.991 (Banks-Baldwin 2001) (emphasis added).[3] The court in *Harris* applied the Ninth Circuit's *Three Valleys* holding, reasoning that:

> the Ninth Circuit addressed the question whether the individual that signed the contract containing the arbitration agreement was actually authorized to sign such a document for the governmental entity. Therefore, the question in *Three Valleys* was whether there ever existed an agreement to arbitrate in the first place. ...
>
> Similarly, in this case, Harris challenges the very existence of the contracts. Harris contends that the contracts are illegal, and, therefore, void and unenforceable.

Harris, 794 So.2d at 316 (citations omitted). *Harris* therefore held that a court must resolve the question of whether a contract containing an arbitration clause is void and non-existent before it can enforce the clause under the FAA. By contrast, the court below referred an identical allegation to arbitration and held that *Three Valleys* is inapplicable. Cert. App. 11. Check Into Cash has not drawn any meaningful distinction that would erase the conflict among these decisions.[4]

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[3] The statute's plain language should put to rest Check Into Cash's concern, Opp. at 18-19, that it does anything but render a contract "void."

[4] Check Into Cash does not even attempt to distinguish *Party Yards, Inc. v. Templeton*, 751 So.2d 121 (Fla. Dist. Ct. App. 2000) and

This Court should grant review to resolve this conflict of federal and state appellate authority over whether *Prima Paint* should be extended to reach allegations that a contract containing an arbitration clause is void *ab initio* and therefore never came into existence and never had any legal effect.

II. The Decision Below is in Tension with this Court's Delineations of Federal Policy under the FAA.

Check Into Cash mis-characterizes the arguments in the petition as an "assault on the efficacy of the FAA and the strong federal policy promoting arbitration" and an "attempt[] to argue *sub silentio* that *Prima Paint* itself was incorrectly decided . . ." Opp. at 7, 10. While this would necessarily implicate the federal and state courts that have embraced our arguments as part of this "assault" on the FAA and *Prima Paint*, these assertions are wholly without merit in any event.

This Court recently held in *Equal Employment Opportunity Comm'n v. Waffle House, Inc.*, __U.S.__, 122 S. Ct. 754 (2002), that an arbitration agreement between an employer and employee did not prohibit the EEOC from suing the employer in court to obtain victim-specific relief for the employee. In recognizing that the arbitration agreement had no effect because the EEOC was not a signatory to the agreement, the Court reaffirmed its recognition that "the FAA is 'at bottom a policy guaranteeing the enforcement of private contractual

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Fastfunding The Co., Inc. v. Betts, 758 So.2d 1143 (Fla. Dist. Ct. App. 2000), both of which required courts to resolve allegations that a contract is void based on its illegal terms before ordering arbitration under the FAA. At the very least, these cases further illustrate the confusion among state and federal courts over the scope of *Prima Paint* and whether the FAA requires arbitration of allegations like those at issue in this case.

arrangements,'" and that the Act "directs courts to place arbitration agreements on equal footing with other contracts." *Id.* at 764 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 625 (1985). Check Into Cash's contention that parties must arbitrate a dispute over the very existence of a contract between them cannot be sustained solely by reference to the FAA's policies when those policies are grounded in the general rules of contract enforcement. A requirement that courts assume the validity of and enforce part of a document that never came into existence as a legal contract runs exactly contrary to the normal approach of contract law.

Nor is Check Into Cash correct in opposing *certiorari* by claiming that the arguments herein would undermine *Prima Paint*. First, *Prima Paint* held that an arbitration clause could be enforced where a party alleged that the contract containing the clause was induced by fraud. The Sixth Circuit below recognized that this fraudulent inducement claim would have rendered a contract "merely voidable," allowing a party to rescind, but would not have voided the contract so that it never had a legal existence in the first place. Cert. App. 8. The difference between a claim that a contract is voidable or revokable and a claim that a contract is void and never came into existence was critical to the findings of the Third and Ninth Circuits that only the latter implicates the making of the arbitration agreement under Section 4 of the FAA and therefore must be resolved by a court *before* it can order arbitration. *See Sandvik*, 220 F.3d at 107; *Three Valleys*, 925 F.2d at 1140. Second, to the extent Check Into Cash is concerned that this argument does undermine *Prima Paint*, the fact that numerous federal and state appellate courts have already embraced the argument would only provide further justification for this Court to grant review on the question presented.

III. The Petition Raises an Important Question of Federal Law that is Properly Presented to the Court.

Check Into Cash raises a number of additional arguments attempting to show that this case presents an inappropriate vehicle for this Court's review. None of these arguments should prevent the Court from granting review on the question presented in this case.

First, the fact that this case "implicates substantive questions of Kentucky State law[,]" Opp. at 18, is irrelevant because the question presented to this Court is purely one of federal law under the FAA. Check Into Cash confuses the state law issue of *whether* its contract is void with the federal law issue of *who decides* whether it is void under the FAA. The petition for *certiorari* presents only the latter question for the Court's review. Indeed, if the state law underpinnings of the former issue did "militate against *certiorari* review," *id.*, then this Court should never have heard *Prima Paint* because that case would have implicated the state law question of whether a contract was induced by fraud. This is not an argument against this Court's exercise of *certiorari* review to decide whether the Federal Arbitration Act requires parties to arbitrate a dispute over the existence of a contract between them.[5]

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[5] Similarly, Check Into Cash's contentions as to the unsettled state of Kentucky law are irrelevant to the issue of who applies that law under the FAA. Even if this discussion were relevant, Respondents' concerns that future legislation may apply to this case while past judicial decisions may not, Opp. at 19, reverses the general principle that "statutes operate only prospectively, while judicial decisions operate retrospectively." *United States v. Security Industry Bank*, 459 U.S. 70, 79 (1982).

Check Into Cash's standing and mootness arguments are also of no avail. Check Into Cash disavows the effect of its arbitration clause on many of the Petitioners, but insists that the clause was signed by and is binding on Petitioner Francine Jackman. Opp. at 2. Ms. Jackson is proceeding individually and as a putative class representative. Since Ms. Jackman disputes the legality of the contract containing this arbitration clause, Check Into Cash should not be heard to argue that she lacks standing to raise the question presented to this Court on behalf of herself and similarly situated putative class members.[6]

Likewise, the fact that the Sixth Circuit remanded other of Petitioners' arguments against arbitration should not prevent this Court from granting review on the issue presented, which the Sixth Circuit most definitely did decide. First, this Court's jurisdiction to review circuit court decisions by writ of *certiorari* is not predicated on a final judgment requirement. *See, e.g., Federal Power Comm'n v. Transcon. Gas Pipeline Corp.*, 423 U.S. 326, 330-31 (1976) (granting review of interlocutory order under 28 U.S.C. § 1254(1)). Second, the fact that other arbitration issues are now before the district court should not deter this Court from granting review because the district court proceedings could be stayed while the case is pending in this Court. Indeed, if the "current posture of the case" is a basis for denying review, *see* Opp. at 20, then Petitioners may never be able to raise the question presented in this Court because any later petition for *certiorari* on this issue

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[6] Check Into Cash's assertion that "this case does not involve a group of individuals with a unity of interest and legal standing to present and argue the claim at issue," Opp. at 21, is neither supported by any legal authority nor does it undermine Ms. Jackman's standing as an individual plaintiff and as a putative class representative to present and argue her claim against Check Into Cash that is indisputably at issue in this case.

would likely be time-barred. *See* SUP. CT. R. 13(1) (petition for writ of *certiorari* must be filed within 90 days of judgment).

Since the question presented is one over which federal and state courts of appeals are sharply divided and the question is properly raised and presented in the petition for *certiorari*, Petitioners respectfully request that the petition be granted.

CONCLUSION

This petition for a writ of *certiorari* should be granted.

Respectfully submitted,

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